Lake Shore Bancorp, Inc.

November 1, 2011

BY ELECTRONIC MAIL
Jennifer J. Johnson, Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue, NW
Washington, DC 20551

RE: Federal Reserve Board's Interim Final Rule on Dividend Waivers by Mutual Holding Companies (Docket No. R-1429 and RIN No. 7100 AD 80)

Dear Ms. Johnson:

We appreciate the opportunity to provide comment to the Board of Governors of the Federal Reserve System in connection with its Interim Final Rule on Dividend Waivers by Mutual Holding Companies (the "Interim Final Rule").

Lake Shore, MHC (the "MHC") is a federally-chartered mutual holding company registered as a savings and loan holding company ("SLHC"), which owns approximately 61.2% of the outstanding common stock of Lake Shore Bancorp, Inc. (the "Company"), a federally-chartered mid-tier stock holding company. Lake Shore, MHC was organized in 2006 and does not engage in any business activity other than holding a majority of the common stock of Lake Shore Bancorp, Inc.

The Company has total assets of $494 million, and is the parent company of Lake Shore Savings Bank (the "Bank"), which is a community bank that operates ten full-service branch locations in Western New York and offers a broad array of retail and commercial lending and deposit services. The Bank was initially chartered as a New York State savings and loan association in 1891 and has had a local presence in Dunkirk, New York since that time. Since 1987, the Bank has opened nine additional branch offices throughout Chautauqua and Erie County, New York. The majority of the Bank's deposits and loans are held by consumers and business owners in the communities it serves within Western New York. During 2006, the Bank was re-organized from a New York State mutual savings and loan charter to the federal stock savings charter.

At the time of the 2006 reorganization, we also completed a minority offering of shares of common stock for sale to our depositors and the general public, which resulted in $27.7 million of capital being raised (net of offering costs). The reorganization gave us the opportunity to

increase our ability to serve our communities, enhance products and services offered to our customers, compete more effectively, enhance our ability to attract and retain qualified directors, management and other employees through stock-based incentive plans, and structure our business in a form that enables us to access the capital markets. In summary, we are a much stronger organization as a result of our mutual holding company formation and minority stock offering.

Since the reorganization, our total equity has increased 125%, from $28.0 million as of December 31, 2005 to $63.0 million as of September 30, 2011. The reorganization has allowed the Company to pay dividends to our shareholders in return for their investment in our company. The Company has paid dividends to our shareholders since November 2006, and these dividends provide our shareholders with a reasonable return for the investment they have made in the Company and the confidence they have in our Bank. Dividends are particularly important for mutual holding company stocks since there is limited capital appreciation associated with a potential change in control. We note that many of the shareholders receiving dividends are the Bank's depositors, borrowers or members of the communities that we serve. The MHC consistently received approval from the Office of Thrift Supervision prior to waiving the receipt of dividends declared by the Company. We believe that the MHC dividend waiver is very beneficial and a key part of an MHC's ability to raise capital and attract investors, as it allows the retention of more capital at both the Company and Bank levels to provide additional strength to the organization.

The Interim Final Rule would restrict, if not prevent, mutual holding companies, like the MHC, from waiving dividends declared by their mid-tier stock holding company or bank subsidiaries and would greatly damage the mutual holding company structure, including the ability of mutual holding companies to raise capital. All of this is being done to avoid a perceived conflict of interest that is extremely difficult to identify based on the very limited rights and interests of mutual members that the United States Supreme Court has said are virtually non-existent. Moreover, the Interim Final Rule would restrict the ability of the MHC to waive dividends despite the fact that we are a "Grandfathered MHC" under Section 625(a) of the Dodd-Frank Act which mandates that the Federal Reserve not object to dividend waivers by Grandfathered MHCs as long as a mutual holding company board determines that the waiver will not be detrimental to the safe and sound operation of the subsidiary savings association and that the waiver is consistent with their fiduciary duties. Nothing in Section 625(a) gives the Federal Reserve the authority to require a depositor or member vote to approve a mutual holding company's decision to waive dividends. Overall, we find that the Interim Final Rule goes well beyond the statutory requirements and intent for dividend waivers by Grandfathered MHCs. Section 625(a) was intended to allow existing federally-chartered mutual holding companies to continue to waive the receipt of dividends under the dividend waiver policies and rules of the OTS which investors had relied on in purchasing common stock of mutual holding company subsidiaries.

The member vote requirement mandated by the Interim Final Rule would be an unnecessary burden on Grandfathered MHCs as the solicitation and tabulation of a member vote to approve the dividend waiver would be very expensive and nearly impossible to obtain. It is important to keep in mind that under the standard of the Interim Final Rule, if a member does not vote, it is the equivalent of a vote against the waiver. Consumers have become very wary of mailings and

home solicitations, and it would be nearly impossible to generate sufficient interest among our members on this issue to receive affirmative responses from at least 50% of our total membership. Such a vote would require our MHC to complete a proxy solicitation involving the mailing of proxy materials to all members and the tabulation of results (in our case, we have 31,000 deposit accounts that would require tabulation). The printing, mailing and tabulation of such a proxy vote would result in a substantial expense that would reduce the Company's net income and negatively impact capital levels at the Company and the Bank.

Again we wish to emphasize that the member vote requirement of the Interim Final Rule would effectively eliminate the ability of mutual holding companies to waive dividends. If the Interim Final Rule is not changed, our Company will be forced to pay dividends to the MHC and the MHC will pay tax on such dividends. This will reduce the capital available to both the Company and Bank, and will diminish the ability of the MHC to act as a "source of strength" to the Bank. Moreover, no benefit will accrue to either the MHC or our members if the MHC receives dividends from the Company. If the MHC cannot waive the receipt of dividends, our minority shareholders would be penalized since the payment to the MHC would be made even though the MHC has not invested in common stock of the Company in the same manner as public shareholders. That is, the shares issued to the MHC were not sold at fair value, and therefore the Company received less capital for such shares than it would have if they were sold at fair value. Preventing the MHC from waiving dividends may require the Company to eliminate cash dividend payments to the Company's minority shareholders, which would damage the Company's goodwill and reputation with our shareholders, depress our stock price in an already depressed and volatile market for financial institution stocks, and negatively impact our ability to raise capital in the future to fund our strategic growth plans. Shareholders who invested in the Company in our minority stock offering relied on the Company's ability to pay dividends and the MHC to waive the receipt of dividends. It is harmful not only to the Company and the Bank, but to all financial institutions that have sold stock and for capital markets in general, for any banking or other regulators to change substantive terms of an investment after the fact. In effect, the Interim Final Rule would take value from our shareholders and damage our Bank.

Furthermore, as noted above, the emphasis in the Interim Final Rule on the rights of mutual members is misplaced and overstated. For a number of reasons, the MHC board of directors believes that the dividend waiver is in the best interest of the MHC, its members and the direct and indirect subsidiaries of the MHC. MHC members, unlike shareholders who have invested risk capital in the Company, have very little interest in voting on MHC matters. Members have no incentive to vote for or against a dividend waiver by the MHC, nor would they receive any benefit from the MHC accepting dividends from the Company. Moreover, the United States Supreme Court has stated at least twice that membership rights in a mutual entity are not equivalent to owning an equity interest in a stock corporation and essentially have no value. The voting rights of mutual members are limited and the framework of the Interim Final Rule expands such rights beyond their historical limitations under federal and state banking laws and regulations. Ultimately, the Interim Final Rule has created an unworkable result that disregards the plain language of the Dodd-Frank Act as well as the intent of Congress. It is largely an affirmation of what many community banks believe to be the Federal Reserve Board's bias against community banks, mutual holding companies and mutual institutions. Moreover, a vote of the mutual members is unnecessary because the members are not adversely affected in any

way by the MHC's dividend waivers. Instead the evidence suggests that dividend waivers have helped our members by allowing our Bank to retain capital, enhance products and services, grow its branch network and offer loans and deposits to members of our local communities, thereby supporting local economic growth. The mutual holding company structure offers converting mutual savings banks the ability to grow and remain independent, which enables them to continue to meet the banking needs of their communities. As such, it provides community banks with a "survival" tool to remain competitive and meet the unique needs of the local consumer and small business person that a larger bank may not be willing to serve.

In our situation, utilizing the mutual holding company structure and issuing minority stock was a more prudent and rational way for us to go public and raise capital in 2006. The structure allowed us to limit the amount of capital raised and provided us with an opportunity to deploy the capital in a reasonable and restrained manner to maintain our community banking identity and remain loyal to the market areas that we serve. Other mutual community banks may find the mutual holding company alternative more viable and practical than the option of becoming a full stock company. The Interim Final Rule, as proposed with its restrictions on mutual holding company dividend waivers, would make the mutual holding company structure less attractive to mutuals and limit the opportunities for such institutions to raise capital. We believe that the Interim Final Rule is counterintuitive as it would limit the capital raising alternatives for mutual institutions in the current weak economic environment where banks are having difficulty raising capital. If the Interim Final Rule stands, it will force mutual holding companies to accept dividends that they do not need, and the safety and soundness of their savings association subsidiaries will be adversely affected by the dissipation of capital in the form of taxes paid by mutual holding companies on dividends received. As noted above, the ownership interests of mutual holding companies in the common stock of their subsidiary holding companies is very different from that of minority shareholders, and the Federal Reserve needs to consider this in its rulemaking.

Lastly, although we are a "Grandfathered" MHC, we believe that the Interim Final Rule should allow non-Grandfathered MHCs to waive the receipt of dividends under the same standards as Grandfathered MHCs outlined in Section 625(a) of the Dodd-Frank Act. We feel the Interim Final Rule requirement for non-Grandfathered MHCs, which requires directors who directly or indirectly own shares of the subsidiary or otherwise benefit from the waiver to abstain from a board vote on mutual holding company dividend waivers, unfairly targets mutual holding companies as uniquely incapable of addressing potential conflicts of interest. Even if one assumes that a substantive conflict of interest exists when a mutual holding company board waives the receipt of dividends, there are numerous other ways to address the conflict, short of prohibiting mutual holding company dividend waivers and irreparably damaging the mutual holding company structure. The Interim Final Rule would have the effect of preventing all non-Grandfathered mutual holding companies from waiving dividends and is entirely unnecessary and excessive. Directors of stock holding companies regularly declare and receive dividends on common stock they own.

Furthermore, the Interim Final Rule should allow "non-Grandfathered" mutual holding companies to waive dividends without diluting minority shareholders in a second step conversion. One solution to the value transfer concern associated with dividend waivers that has

been expressed by the Federal Reserve is to simply require that the amount of waived dividends be added to a liquidation account created when the mutual holding company converts to stock form, in precisely the same way that the pre-conversion equity of a mutual institution is not distributed to members but added to a liquidation account in the converted stock bank at the completion of the conversion.

Treating "non-Grandfathered MHCs" in a different manner than Grandfathered MHCs is discriminatory and confusing to minority shareholders who have invested risk capital in a mutual holding company.

We would appreciate it if you would consider the points we have noted above and reconsider the provisions of the Interim Final Rule. We strongly believe that the mutual holding company structure provides value to the banking system in the United States and is a viable alternative for community bank mutual institutions interested in raising capital. If the mutual holding company alternative is no longer viable for mutual institutions, many community banks may no longer be able to remain competitive in the current economic and regulatory environment.

Thank you for the opportunity to comment on this proposed rule. If you have any questions concerning our letter, please feel free to contact us at (716) 366-4070.

Sincerely,

Daniel P. Reininga
President and Chief Executive Officer

Rachel A. Foley
Chief Financial Officer